Probate Avoidance Strategies

With the changes to Ontario Estate Administration Tax Act [the EAT], which is the legislation that imposes what is commonly referred to as the "probate fee", and the Department of Finance's proposed changes to the taxation of testamentary trusts, more people should be incorporating probate avoidance strategies in their estate planning.

The avoidance of Ontario's EAT is surprisingly easy to achieve. If your estate can avoid the probate process, then you have avoided the EAT. Success largely depends on the nature of the assets owned and how aggressive and careful the client is in structuring their affairs.

The potential advantages of planning to avoid probate

-speed in administration and distribution
-avoidance of payment of Ontario's Estate Administration Tax
-avoidance of compliance costs for the EAT, eg, legal costs, appraisal costs, costs associated with delays in final distribution resulting from the EAT.

The problem with many avoidance plans is that they are not well thought out and documented. Sometimes the result is they are simply ineffective, but, more importantly, they may result in unintended consequences, delays in administration, and in the worst cases, family disputes and lawsuits. The following is a brief discussion of some common probate avoidance strategies.

Joint Ownership

Whether real estate or financial assets, joint ownership is the most common tool used to avoid probate. Unfortunately, the common law applies presumptions to these forms of ownerships and too often they result in unintended results, which result in delays and expensive litigation. Indeed, there are simply too many recently reported court cases dealing with Jointly owned assets. For example, as between husband and wife, joint ownership will generally result in what is termed a "presumption of advancement". In other words, in creating the joint account, the deceased intended to benefit their spouse by advancing their interest and acquiring sole ownership on death. In all other cases, for example, where it is intended to assist in the transfer of assets to children, there will likely be a presumption that the survivor holds the funds as a Trustee. If there is no other evidence relating to the deceased person's intention, there will likely be a trust for the deceased person's estate. In turn, the assets are likely still subject to probate.

There are also issues that can arise prior to death. For example, if the jointly held property is a residence, what is the status of the Income Tax principal residence exemption? With any asset held jointly, what happens if the added joint owner goes bankrupt or has a marriage failure? If the assets are subject to capital gains tax, does the transfer trigger an immediate tax liability?

Leaving properly drawn documents evidencing what the deceased intended by the transfer or creation of the joint interest should avoid the often devastating complications

associated with the litigation that ensues after death in these situations. Even where litigation does not result, I have seen instances where the beneficiary named on the joint account has used the final disposition of the assets as leverage with other family members with resultant damage to family relations.

If there is no clear documentation that the joint account is not held on resulting trust for the estate, then the estate trustee may even be under a legal obligation to both include the funds in the EAT [probate] calculation, and take legal action to recover the funds and include them in the estate accounts.

Designated Beneficiaries

There are numerous financial vehicles which permit you to name a beneficiary in event of death, for example, Registered Retirement Savings Plans, Registered Retirement Income Funds, Tax Free Savings Accounts, Life Insurance policies, and virtually any investment issued by an insurance company. Properly done, these designations allow for timely and cost effective settlement of estate assets. Improperly done, they may result in significant unintended consequences. For example, a person who leaves a Registered Retirement fund that names an adult child as beneficiary risks all the funds passing to the named child, but the significant tax bill from the de-registration of the fund on death, going to the estate. The result can be significant distortion of the estate distribution resulting in unintended results. Again, litigation amongst family members with its attendant risks, delays, and costs is a significant risk.

The solution is a detailed plan which anticipates how the naming of the beneficiary impacts the total estate and its taxation is the solution. The simple naming of the beneficiary may not be sufficient, but an agreement with the named beneficiary or a trust declaration which binds that beneficiary may be a cost effective solution.

Double Wills

The structure of some estates lends them to having one Will for assets subject to probate and one Will for assets not subject to probate. The most common example is shares in private corporations. The directors of a private corporation have a discretion to waive probate in the event of death of a shareholder. Frequently, the corporation will also owe this shareholder funds represented by promissory notes. Again, the directors of the company can consent to the transfer of the promissory note to beneficiaries without requiring probate.

More aggressive uses may exist for the double Will strategy for those prepared to explore detailed planning for their estate.

Alter Ego and Joint Partner Trusts

People 65 and older may wish to consider the use of trusts which comply with the rules in the Income Tax Act relating to Alter Ego Trusts and Joint Partner trusts. Essentially the senior transfers their assets to a trust during their retirement years, which then administers the assets during their lifetime and after death. On death, the trust simply distributes the assets to the

beneficiaries named in the Trust document. The Will, while still necessary, becomes primarily an administrative tool and a safety net for assets which may have been missed in establishing the trust or subsequently acquired.

The Alter Ego and Joint Partner Trust may be a more effective tool than a Power of Attorney, for those wishing to anticipate mental frailty. A person can be their own Trustee, or one of them, while still competent, and the use of family members as co-trustees or alternative trustees can keep the costs of maintaining the trust very reasonable.

While Alter Ego and Joint Partner Trusts have seen limited use in the past, the combined effect of the changes to the EAT and proposed changes to the taxation of testamentary trusts may make Alter Ego and Joint Partner trusts one of the best estate planning tools of the future. A more detailed discussion of the advantages of Alter Ego and Joint Partner Trusts can be found here.

Information about the Probate process is also available from the Ministry of the Attorney General's website here.